

**LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE**

**CONSOLIDATED FINANCIAL STATEMENTS
AND AUDITOR'S REPORT**

JUNE 30, 2016

**LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE**

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**Independent Auditor's Report on Consolidated Financial Statements
and Supplementary Information**

**Board of Directors
Leake and Watts Services, Inc.
and Affiliate**

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Leake and Watts Services, Inc. and Affiliate, which comprise the consolidated statement of financial position as of June 30, 2016 and the related consolidated statements of activities and cash flows for the year then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We did not audit the financial statements of The Emergency Shelter, Inc., a related entity, which statements reflect total assets constituting 3.8% percent of consolidated total assets and total revenues constituting 0% of consolidated total revenues for the year then ended. Those statements were audited by other auditors, whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for The Emergency Shelter, Inc., is based solely on the report of the other auditors. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, based on our audit and the report of the other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Leake and Watts Services, Inc. and Affiliate as of June 30, 2016, and the changes in their net assets and their cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

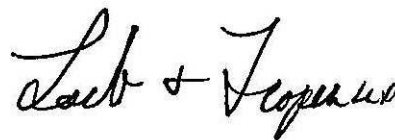
Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The information as of and for the year ended June 30, 2016 included in Schedules 1 through 3 is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, based on our audit and the report of the other auditors, the information as of and for the year ended June 30, 2016 is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

Report on Summarized Comparative Information

We have previously audited Leake and Watts Services, Inc. and Affiliate's June 30, 2015 consolidated financial statements, and we expressed an unmodified audit opinion on those audited financial statements in our report dated November 25, 2015. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2015 is consistent, in all material respects, with the audited consolidated financial statements from which it has been derived.

We had also expressed an unmodified opinion on the supplementary information included in Schedules 1 through 3 for the year ended June 30, 2015 in relation to those consolidated financial statements as a whole. In our opinion, the 2015 supplementary information in Schedules 1 through 3 is consistent, in all material respects, with the audited supplementary information from which it has been derived.



December 1, 2016

**LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE**

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

JUNE 30, 2016

(With Summarized Financial Information for June 30, 2015)

	2016	2015
ASSETS		
Current assets		
Cash and cash equivalents	\$ 3,091,604	\$ 2,324,191
Investments (Note 3)	7,237,695	12,106,477
Investments - certificates of deposit	25,000	25,000
Accounts receivable (net of allowance of \$319,000)	10,157,586	10,657,638
Other receivables	186,965	298,122
Prepaid expenses	640,855	627,809
Accrued investment interest receivable	32,262	40,729
Total current assets	21,371,967	26,079,966
Assets limited as to use - investments (Notes 3 and 8)	639,057	1,389,032
Other assets		
Investments (Note 3)	2,361,096	861,096
Security deposits	105,727	36,027
Beneficial interest in perpetual trusts (Notes 3 and 14)	1,436,906	1,525,574
Deferred financing costs (Notes 6 and 8)	968,885	1,072,698
Fixed assets - net (Note 4)	34,202,984	34,153,210
Total other assets	39,075,598	37,648,605
Total assets	\$ 61,086,622	\$ 65,117,603

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**LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE**

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

JUNE 30, 2016

(With Summarized Financial Information for June 30, 2015)

	<u>2016</u>	<u>2015</u>
LIABILITIES AND NET ASSETS		
Current liabilities		
Accounts payable	\$ 3,277,851	\$ 3,381,699
Accounts payable - construction		623,244
Accrued payroll and employee benefits (Notes 9 and 10)	3,962,620	2,869,078
Accrued expenses and other liabilities (Note 10)	3,658,063	3,141,466
Advances from government agencies	2,117,721	4,775,822
Accrued interest payable	42,744	45,544
Line of credit and notes payable (Note 6)	743,483	2,713,790
Capital leases payable (Note 7)	56,147	46,737
Bonds payable - net (Note 8)	1,606,000	1,689,000
	<u>15,464,629</u>	<u>19,286,380</u>
Total current liabilities		
Long-term liabilities		
Accrued payroll and employee benefits (Note 10)	465,549	515,113
Line of credit and notes payable (Note 6)	7,544,240	8,127,690
Capital leases payable (Note 7)	92,509	33,596
Bonds payable - net (Note 8)	20,381,712	21,984,522
	<u>28,484,010</u>	<u>30,660,921</u>
Total long-term liabilities		
Total liabilities	<u>43,948,639</u>	<u>49,947,301</u>
Net assets (Exhibit B)		
Unrestricted	13,198,603	10,980,803
Temporarily restricted (Note 11)	141,378	302,829
Permanently restricted (Note 14)	3,798,002	3,886,670
	<u>17,137,983</u>	<u>15,170,302</u>
Total net assets		
Total liabilities and net assets	<u>\$ 61,086,622</u>	<u>\$ 65,117,603</u>

See independent auditor's report.

The accompanying notes are an integral part of these statements.

**LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE**

EXHIBIT B

CONSOLIDATED STATEMENT OF ACTIVITIES

**YEAR ENDED JUNE 30, 2016
(With Summarized Financial Information
for the Year Ended June 30, 2015)**

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>	
				<u>2016</u>	<u>2015</u>
Operating revenues					
Program revenue (Note 5)	\$ 86,299,264			\$ 86,299,264	\$ 81,139,330
In-kind contributions	470,609			470,609	637,985
Program development grant	4,347,952			4,347,952	
	<u>91,117,825</u>			<u>91,117,825</u>	<u>81,777,315</u>
Total operating revenues					
Operating expenses (Schedule 3)					
Program services					
Child Welfare	29,918,264			29,918,264	28,048,759
Special Education	17,809,935			17,809,935	18,073,954
Developmental Disabilities	12,214,129			12,214,129	11,610,484
Early Childhood	12,242,168			12,242,168	12,101,127
Juvenile Justice	10,282,912			10,282,912	6,905,741
	<u>82,467,408</u>			<u>82,467,408</u>	<u>76,740,065</u>
Total program services					
Supporting services					
Management and general	8,215,484			8,215,484	6,396,899
Development	273,428			273,428	223,644
	<u>8,488,912</u>			<u>8,488,912</u>	<u>6,620,543</u>
Total supporting services					
Total operating expenses (includes interest expense of \$1,408,650)	<u>90,956,320</u>			<u>90,956,320</u>	<u>83,360,608</u>

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**LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE**

**EXHIBIT B
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CONSOLIDATED STATEMENT OF ACTIVITIES

**YEAR ENDED JUNE 30, 2016
(With Summarized Financial Information
for the Year Ended June 30, 2015)**

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>	
				<u>2016</u>	<u>2015</u>
Change in net assets from operations	\$ 161,505			\$ 161,505	\$ (1,583,293)
Nonoperating revenues and expenses					
Investment income (loss) (Note 3)	(13,017)			(13,017)	333,926
Capital improvement grant	645,974			645,974	
Contributions	793,304	\$ 116,378		909,682	971,647
Special events	474,647			474,647	621,668
Direct costs of special events	(122,557)			(122,557)	(109,702)
Change in value of beneficial interest in perpetual trusts			\$ (88,668)	(88,668)	23,973
Miscellaneous income	115			115	133
Net assets released from restrictions (Note 11)	<u>277,829</u>	<u>(277,829)</u>			
Change in net assets (Exhibit C)	2,217,800	(161,451)	(88,668)	1,967,681	258,352
Net assets - beginning of year	<u>10,980,803</u>	<u>302,829</u>	<u>3,886,670</u>	<u>15,170,302</u>	<u>14,911,950</u>
Net assets - end of year (Exhibit A)	<u>\$ 13,198,603</u>	<u>\$ 141,378</u>	<u>\$ 3,798,002</u>	<u>\$ 17,137,983</u>	<u>\$ 15,170,302</u>

See independent auditor's report.

The accompanying notes are an integral part of these statements.

**LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE**

CONSOLIDATED STATEMENT OF CASH FLOWS

YEARS ENDED JUNE 30, 2016 AND 2015

	<u>2016</u>	<u>2015</u>
Reconciliation of change in net assets to net cash provided by operating activities		
Change in net assets (Exhibit B)	\$ 1,967,681	\$ 258,352
Adjustments to reconcile change in net assets to net cash provided by operating activities		
Depreciation and amortization	2,535,937	2,135,860
Amortization of bond issuance costs	103,813	98,071
Amortization of bond discount	(3,190)	(3,191)
Realized (gains) losses on investments	139,675	(33,363)
Unrealized (gains) losses on investments	98,569	(87,624)
Change in value of beneficial interest in perpetual trusts	88,668	(23,973)
Donated securities	(25,496)	(8,001)
Decrease (increase) in assets		
Accounts receivable	562,052	(2,480,199)
Other receivables	111,157	37,985
Prepaid expenses	(13,046)	(151,232)
Accrued investment interest receivable	8,467	(722)
Security deposits	(69,700)	16,329
Increase (decrease) in liabilities		
Accounts payable	(103,848)	(153,603)
Accrued payroll and employee benefits	1,043,978	(114,822)
Accrued expenses and other liabilities	516,597	484,152
Advances from government agencies	(2,658,101)	4,775,822
Accrued interest payable	(2,800)	(2,294)
	<u>4,300,413</u>	<u>4,747,547</u>
Cash flows from investing activities		
Purchase of investments	(8,584,268)	(13,896,153)
Proceeds from sale of investments	11,740,302	14,415,710
Loan to post employment benefit trust	(62,000)	(64,000)
Decrease in investments limited as to use	749,975	70,245
Fixed asset acquisitions	(3,088,387)	(5,338,020)
	<u>755,622</u>	<u>(4,812,218)</u>

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**LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE**

CONSOLIDATED STATEMENT OF CASH FLOWS

YEARS ENDED JUNE 30, 2016 AND 2015

	<u>2016</u>	<u>2015</u>
Cash flows from financing activities		
Payments of line of credit and notes payable	\$ (9,698,857)	\$ (6,184,681)
Proceeds from line of credit and notes payable	7,145,100	7,700,000
Payments on bonds payable	(1,682,620)	(1,471,618)
Principal payments on capital lease	<u>(52,245)</u>	<u>(42,687)</u>
Net cash provided (used) by financing activities	<u>(4,288,622)</u>	<u>1,014</u>
Net change in cash and cash equivalents	767,413	(63,657)
Cash and cash equivalents - beginning of year	<u>2,324,191</u>	<u>2,387,848</u>
Cash and cash equivalents - end of year	<u>\$ 3,091,604</u>	<u>\$ 2,324,191</u>
Supplemental disclosure of cash flow information		
Cash paid during the year for interest	<u>\$ 1,411,450</u>	<u>\$ 1,094,362</u>
Noncash transactions related to the acquisition of a term loan and line of credit from TD Bank		
The following were paid through direct financing:		
Payment of line of credit and notes payable		\$ (7,571,656)
Payments of interest		(11,280)
Deferred financing costs		(60,512)
Capital lease acquisition	\$ 120,568	

See independent auditor's report.

The accompanying notes are an integral part of these statements.

**LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 1 - NATURE OF ORGANIZATION

Leake and Watts Services, Inc. provides comprehensive social services including family stabilization, foster care, child care and Head Start, residential and respite services for children and adults with developmental disabilities, special education, residential treatment and group homes for youth with emotional and mental health challenges and a spectrum of residential and treatment services for adjudicated youth and youth awaiting court action. Most families served live throughout New York City and Westchester County. The primary sources of revenue are the New York City Administration for Children's Services and various New York State government agencies.

The Emergency Shelter, Inc. alleviates human suffering and distress through programs that feed, house, shelter, and train homeless and unemployed men, women and youth. The primary source of funding is income associated with the organization's beneficial interests in perpetual trusts held by third parties.

Leake and Watts Services, Inc. is related to The Emergency Shelter, Inc. through common board control. Leake and Watts received \$75,000 from The Emergency Shelter, Inc. for certain services that Leake and Watts has provided. The Emergency Shelter, Inc. is consolidated in these financial statements.

Leake and Watts Services, Inc. and its Affiliate ("Leake and Watts") are each exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code.

- **Child Welfare** programs and services.
 - The **Residential Treatment Center**, located on a 30-acre campus in Yonkers, provides 24-hour residential care to youth ages 12-21 requiring more significant therapeutic and educational support. An enriched, structured program of activities coupled with clinical services assists youth with mental health concerns and challenging behaviors to develop the ability to participate fully in the surrounding community and to return to a less restrictive environment. Some of the youth served at the Residential Treatment Center are in foster care.
 - The **Family Foster Care** program serves children who have experienced abuse and neglect. The goal in all cases is to establish a permanent appropriate living arrangement for the child, preferably back with his/her birth family. If that is not possible, the goal is to establish a home with an adoptive family or to prepare the youth to live independently.
 - Our evidence-based **Multidimensional Treatment Foster Care (MTFC)** serves teens in foster care with emotional and behavioral challenges with more intensive supports.

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**LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 1 - NATURE OF ORGANIZATION (continued)

- Our **Mother/Child home** in the Bronx serves teen mothers in foster care along with their children. The focus, as with all foster youth, is on education, skills development (with particular emphasis on parenting skills training), employment, safety and well-being.
- **Preventive Services Programs** strengthen and preserve families, keep children safe by preventing child abuse and neglect, and prevent the necessity of placing children in foster care utilizing two evidence-based models that have proven track records of success, Family Connections and Functional Family Therapy - Child Welfare adaptation.
- Our **Passage of Hope (POH)** program serves undocumented migrant children (mostly from Honduras, El Salvador and Guatemala) who have come into the United States without an adult guardian. These children are temporarily taken into the custody of the Department of Health and Human Services, Office of Refugee Resettlement, and placed with us so they may receive a myriad of services (medical, clinical, education, legal, etc.) while they are reunified with their families in the U.S.
- Youngsters in our child welfare programs also receive services and referrals from our **Clinic** to ensure that their health and mental health needs are met.
- **Special Education** services to school-age children through both The Biondi School and at our Residential Treatment Center.
 - Many students have a history of mental health challenges, learning disabilities, substance abuse, general delinquency, depression, psychotic thinking, suicidal ideation, impulsivity, anxiety and poor social skills. **The Biondi School** is a non-public school providing 12-month specialized educational services. Emphasis is on academic achievement, skills development, and increasing each student's ability to remain on task, interact appropriately with peers, and improve behavior so that they can return to their local public school.
- **Developmental Disabilities Services** include community-based programs such as community residences and supported apartments, prevocational services, supportive employment, day habilitation services, and Medicaid Service Coordination for both children and adults. Our supportive clinical practices address the associated emotional, behavioral and psychological issues/disorders in order to assist our consumers to live more fulfilling lives.

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**LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 1 - NATURE OF ORGANIZATION (continued)

- **Community School Services**, in collaboration with the NYC Department of Education, work with two middle schools in the Bronx. Educators, Leake and Watts staff and families share leadership and organize resources so that academics, social services and other supports are integrated into the fabric of each school. These combined supports help the schools better address the needs of young people, resulting in improved student learning, stronger families, and healthier communities.
- **Early Childhood Centers** for children ages 18 months to 5 years.
 - Program components include an early childhood educational curriculum which prepares children for their school years promoting creativity, pre-academic skills, socialization, and independence, bilingual (Spanish) services, parent involvement, and linkage to community and social services.
 - Located in the Bronx, our federally funded **Head Start** program serves children and families living at or below the poverty level and our **Early Head Start** program serves pregnant women, infants and toddlers. The **Seabury Day Care** Center provides early education services to children from low-income, working families.
 - The **Brownell Preschool** and **Ames Early Childhood Center** serve both typically developing children with UPK services as well as those in need of preschool special education services in integrated as well as segregated classes, depending on the need of the child.
 - The **Children's Learning Center** provides preschool special education to children with intensive needs in small classes.
 - The **Family Resource Center** provides a wide range of free services to children and families in the Soundview section of the Bronx. Services include: Computer lab, recreational activities for families, infant and toddler play groups, parent support groups, money management workshops, assistance connecting to Adult Education programs and additional social services.
- Our **Parent-Child Home Program** provides support to low-income families in the Bronx with children ages 18 months to 33 months. This evidence-informed, early childhood home-visiting program focuses on developing pre-literacy skills to promote school readiness, promoting positive parenting skills, building positive child-parent interactions, and enhancing children's social and emotional development.

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**LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 1 - NATURE OF ORGANIZATION (continued)

- **Juvenile Justice** Services include secure to non-secure placement programs for court-involved youth, all of which are based on the belief that young people with histories of delinquency need support, education and other tools to return safely and successfully to their communities and break the cycle of delinquency.
 - **Woodfield Facility** is a secure detention center for youth under the age of 16 who are awaiting court action. These youth are accused of committing crimes, some of which are violent in nature. Services include individual and group counseling, a full-day school program, 24-hour medical services, family outreach, aftercare planning, and religious and spiritual services. These services are offered in a structured setting and a caring, albeit high-security, environment.
 - Our **Limited Secure Placement** program (LSP) is a residential program serving adjudicated youth ages 14 to 18 (and on occasion, an older or younger youth may be served). Both general and specialized populations are served. We ensure that youth are able to develop their academic, pre-vocational and communications skills through various aspects of the program and work with family members to maintain and strengthen the youth's connection with his or her family and community. Aftercare services are also provided to youth around New York City who are transitioning out of LSP programs.
 - Our **Non-Secure Placement** program is also part of the residential care continuum for adjudicated Juvenile Delinquents in New York City ages 12 to 14. Our program is community-oriented and family-focused, using the nationally recognized treatment method, the Missouri Model, that involves grouping youth into small cohorts of 10-12 with whom they live, attend school, participate in recreational activities and receive counseling.
 - The **Family Respite** program serves youth ages 7 to 17 who are at risk of contact with the juvenile justice system by providing respite services for up to 21 days. The program staff also refers families to appropriate community-based services for sustained assistance.
 - **Managed Care** services were in development in FY16 and will be fully implemented in FY17. The source of revenue for Managed Care services is Medicaid, Medicaid Managed Care, Medicare, and Medicare Managed Care.

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**LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 1 - NATURE OF ORGANIZATION (continued)

- An **Article 31 Clinic** will provide outpatient mental health treatment to children and adolescents ages 5 to 21 years and their family members who meet criteria for a mental health diagnosis under DSM5.
- **Health Home** will enable Leake and Watts to serve as a downstream Care Management Agency (CMA) providing comprehensive care management services to children and adults who meet necessary criteria.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation - The financial statements of Leake and Watts have been prepared on the accrual basis of accounting.

Basis of consolidation - All material intercompany transactions and balances are eliminated in the consolidation.

Use of estimates - The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and cash equivalents - Leake and Watts considers highly liquid investments with original maturities, when acquired, of 90 days or less to be cash equivalents.

Investments - Investments are recorded at fair value. Leake and Watts invests in various securities. Investment securities, in general, are exposed to various risks such as interest rate, credit, and overall market volatility risk. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in the values of investment securities will occur in the near term, based on the markets' fluctuations, and that such changes could materially affect the amounts reported in the financial statements.

Investments - certificates of deposit - Certificates of deposit with maturities greater than three months when originally acquired are considered investments for cash flow purposes.

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**LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Accounts receivable, other receivables and program revenue - Leake and Watts records receivables and revenue when earned based on established rates and contracts for service provided. Government grants are recorded as revenues to the extent that expenses have been incurred for the purposes specified by the grantors. Revenues received from government agencies are subject to audit by such agencies. Laws and regulations related to government programs are subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates may change by a material amount in the near term. Additionally, noncompliance with such laws and regulations could result in fines, penalties and exclusion from the government programs. Interest is not charged on outstanding receivables.

Allowance for doubtful accounts - Leake and Watts determines whether an allowance for uncollectibles should be provided for accounts receivable. Such estimates are based on management's assessment of the aged basis of its sources, current economic conditions and historical information. Accounts receivable are written off against the allowance for doubtful accounts when all reasonable collection efforts have been exhausted.

Fair Value Measurements

Fair Value Measurements establishes a framework for measuring fair value. The framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are described below. Level 1 inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that Leake and Watts has the ability to access. Level 2 inputs to the valuation methodology include:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets or liabilities in inactive markets;
- Inputs other than quoted prices that are observable for the asset or liability;
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

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**LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Fair Value Measurements (continued)

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability. Level 3 inputs to the valuation methodology are unobservable and significant to the fair value measurement. The asset or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

The following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used at June 30, 2016 as compared to those used at June 30, 2015.

- *Fixed-income securities (other than mutual funds and mortgage-backed securities)* - Valued at the closing price reported on the active market on which the individual securities are traded.
- *Mortgage-backed securities* - Valued using pricing models maximizing the use of observable inputs for similar securities. This includes basing value on yields currently available on comparable securities of issuers with similar credit ratings.
- *Mutual funds* - Valued at the net asset value (NAV) of shares held at end of year.
- *Beneficial interests in perpetual trusts* - Beneficial interests in perpetual trusts are valued at fair value of The Emergency Shelter, Inc.'s beneficial interests in the fair value of underlying assets.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while Leake and Watts believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

See Note 3 for the tables that set forth by level, within the fair value hierarchy, the assets at fair value.

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**LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Fixed assets - Fixed assets having a useful life greater than one year and costing \$5,000 or more, are stated at cost or fair market value. Depreciation is computed on the straight-line basis over the estimated useful lives of the assets. Capital leases and leasehold improvements are amortized over either the remaining term of the underlying lease or the useful lives of the improvements, whichever is shorter, using the straight-line method.

The estimated useful lives of such assets are as follows:

Building and building improvements	10 to 40 years
Furniture, fixtures and equipment	3 to 10 years
Leasehold improvements	3 to 20 years

Assets limited as to use - Investments whose assets are set aside under the terms of various bond agreements as well as the Replacement Reserve Fund. The Replacement Reserve Fund is used specifically for repair and maintenance of New York State Office for People With Developmental Disabilities (OPWDD) - funded IRA residences.

Beneficial interests in perpetual trusts - The Emergency Shelter, Inc. has beneficial interests in various perpetual trusts. The Emergency Shelter, Inc.'s interest in these trusts is reported as a contribution in the year received at their fair value. Changes in the fair value of the underlying assets are recorded as revenue adjusting permanently restricted net assets.

Advances from government agencies - Advances from government agencies consists of cash received from various government agencies in advance of allowable expenses being incurred.

Deferred financing costs - deferred financing costs are recorded at cost and are amortized using the straight-line basis over the term of the related debt.

Net assets - Net assets are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of Leake and Watts are classified and reported as follows:

Unrestricted - Unrestricted net assets include funds having no restrictions as to use or purpose imposed by donors.

-continued-

**LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Net assets (continued)

Temporarily restricted - Net assets that are subject to donor-imposed stipulations that will be met by either the actions of Leake and Watts and/or the passage of time. Temporarily restricted revenue earned and expended in the same fiscal year is reflected as unrestricted revenue.

Permanently restricted - Net assets that have been restricted by donors to be maintained in perpetuity. Investment income earned in relation to permanently restricted endowments is initially classified as temporarily restricted net assets and is recorded as unrestricted upon expenditure for the program for which the endowment fund was established.

Contributions - Unconditional contributions, including promises to give cash and other assets, are recorded at fair value at the date the contribution is received. Leake and Watts reports gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or a purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions. Donated fixed assets that are restricted for use in specific programs are released from restriction over the useful lives of the assets.

Government grants - Leake and Watts records revenue from expense based reimbursement grants as earned.

Contributed costs and revenues - Leake and Watts operates programs where certain costs including facility costs, fringe benefits for staff, and consumable supplies are paid directly by New York City. Leake and Watts reports these amounts as operating revenues and expenses, and recognized \$470,609 of contributed costs.

Measure of operations - Leake and Watts' change in net assets from operations includes revenues and expenses directly related to the provision of program services. Investment income, capital improvement grant, contributions, both restricted and unrestricted, special events and related direct costs, bond cost write off, change in value of beneficial interests in perpetual trusts, and miscellaneous income are considered nonoperating.

Operating leases - Rent lease expense has been recorded on the straight-line basis over the term of the lease. Deferred rent is recorded if material.

-continued-

**LEAKE AND WATTS SERVICES, INC.
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Functional allocation of expenses - The costs of providing services have been summarized on a functional basis. Accordingly, certain costs have been allocated among the programs and supporting services benefited.

Summarized financial information - The financial statements include certain prior-year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with Leake and Watts' financial statements for the year ended June 30, 2015, from which the summarized information was derived. To conform to the current year presentation certain June 30, 2015 financial statements amounts have been reclassified:

- \$308,513 reported as other operating revenue have been reclassified as program revenue
- \$36,027 reported as prepaid expenses have been reclassified as security deposits
- \$637,985 reported as program revenue have been reclassified as in-kind contributions

Uncertainty in income taxes - Leake and Watts has determined that there are no material uncertain tax positions that require recognition or disclosure in the consolidated financial statements. Periods ending June 30, 2013 and subsequent remain subject to examination by applicable taxing authorities.

Subsequent events - Subsequent events have been evaluated through December 1, 2016, which is the date the consolidated financial statements were issued.

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**LEAKE AND WATTS SERVICES, INC.
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 3 - INVESTMENTS AND BENEFICIAL INTERESTS IN PERPETUAL TRUSTS

Unrestricted and permanently restricted investments, assets limited as to use and beneficial interests in perpetual trusts, as described in Note 2, are included in the following tables set forth by level, within the fair value hierarchy at fair value:

	Level 1			Level 2			Level 3	Total
	Investments	Assets Limited As To Use	Total	Investments	Assets Limited As To Use	Total		
Investments at fair value								
Fixed-income securities								
U.S. Treasury obligations	\$ 1,222,834	\$ 227,161	\$ 1,449,995					\$ 1,449,995
Mortgage-backed securities				\$ 8,998		\$ 8,998		8,998
Municipal authorities	150,017		150,017					150,017
Corporate bonds								
Telecommunications	277,789		277,789					277,789
Energy	81,739		81,739					81,739
Finance	882,065		882,065					882,065
Consumer goods	444,286		444,286					444,286
Services	129,326		129,326					129,326

-continued-

**LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 3 - INVESTMENTS AND BENEFICIAL INTERESTS IN PERPETUAL TRUSTS (continued)

	Level 1			Level 2			Level 3	Total
	Investments	Assets Limited As To Use	Total	Investments	Assets Limited As To Use	Total		
Mutual funds								
Large cap	\$ 3,975,357		\$ 3,975,357					\$ 3,975,357
Mid cap	805,444		805,444					805,444
Small cap	532,068		532,068					532,068
International-developed	672,783		672,783					672,783
Equity REITS	199,217		199,217					199,217
Other equity	<u>61,010</u>		<u>61,010</u>					<u>61,010</u>
Total investments reported on the fair value hierarchy	9,433,935	\$ 227,161	9,661,096	\$ 8,998		\$ 8,998		9,670,094
Cash equivalents	<u>155,858</u>	<u>411,896</u>	<u>567,754</u>					<u>567,754</u>
Total investments	<u>\$ 9,589,793</u>	<u>\$ 639,057</u>	<u>\$10,228,850</u>	<u>\$ 8,998</u>	<u>\$ -</u>	<u>\$ 8,998</u>		<u>\$10,237,848</u>
Beneficial interests in perpetual trusts							<u>\$ 1,436,906</u>	<u>\$ 1,436,906</u>

-continued-

**LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

**NOTE 3 - INVESTMENTS AND BENEFICIAL INTERESTS IN PERPETUAL TRUSTS
(continued)**

Included in investments is \$2,361,096 of permanently restricted funds.

Included in assets limited as to use is \$78,005 of replacement fund for residences.

The following table sets forth the changes in the Level 3 assets:

	<u>Beneficial Interest in Perpetual Trusts</u>
Beginning balance	\$ 1,525,574
Total gains (losses) (realized/unrealized) included in changes in net assets for the year ended June 30	<u>(88,668)</u>
Ending balance	<u>\$ 1,436,906</u>
The amount of total gains (losses) for the period included in changes in net assets attributable to the change in unrealized gains (losses) relating to assets still held at the reporting date	<u>\$ (88,668)</u>

Investment income (losses) consists of the following:

Interest and dividend income	\$ 297,154
Realized losses	(139,674)
Unrealized losses	(98,569)
Investment expenses	<u>(71,928)</u>
Investment income (loss)	<u>\$ (13,017)</u>

-continued-

**LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 4 - FIXED ASSETS

Fixed assets consist of the following:

Land	\$ 38,787
Building and building improvements	53,072,001
Leasehold improvements	5,680,881
Furniture, fixtures and equipment	7,762,577
Construction in progress	<u>3,338,065</u>
 Total cost	 69,892,311
 Less accumulated depreciation and amortization	 <u>(35,689,327)</u>
 Fixed assets - net	 <u>\$ 34,202,984</u>

Equipment costing \$342,103 and associated accumulated amortization of \$134,777 are subject to capital lease agreements as described in Note 7.

NOTE 5 - REVENUE RECOGNITION AND ADJUSTMENTS

Revenues are recognized when earned as services are performed and are based on rates, fees for services and contractual agreements with various Federal, New York State, New York City, Westchester County and other public agencies.

Revenues under third-party-payor agreements are subject to audit and potential retroactive adjustments. Provisions for estimated third-party-payor settlements are recorded in the period when the services are rendered. Differences between the estimated amounts accrued, interim and final settlements are reported in operations in the year of determination.

-continued-

**LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 5 - REVENUE RECOGNITION AND ADJUSTMENTS (continued)

Reimbursement methodologies for some of the major programs present at Leake and Watts are as follows:

Education and Early Childhood

Leake and Watts' school programs are regulated and funded by the New York State Education Department. A tuition rate per student is established based upon enrollment, actual cost data, geographic location and other cost "screens" prescribed by the State. Fluctuations in enrollment and costs can have a significant impact on Leake and Watts' receipt of a rate sufficient to cover program costs. Revenue from support payments from the New York City Department of Education (NYC-DOE) is subject to final reconciliation. Revenue and support payments have been reconciled with the NYC-DOE through the fiscal year ended June 30, 2012.

Foster Care, Residential Treatment and Medical and Mental Health Services

The principal source of revenue consists of support payments received from the City of New York (the "City") and Westchester County for congregate and foster boarding home care, and health care provided to children referred to Leake and Watts. Such payments, based initially upon per diem rates established annually by the New York State Office of Children and Family Services (NYS-OCFS), the New York City Administration for Children's Services (NYC-ACS), and the State Department of Health, are finalized after the reported costs and days of care are audited. Revenue for support payments from NYC-ACS is subject to audit.

Developmental Disabilities Services

Developmental Disabilities Services including community-based programs such as group homes and supported apartments, respite/recreation services, supportive employment, day services, and Medicaid Service Coordination are funded through contracts with OPWDD and by Medicaid, based on rates established by OPWDD.

NOTE 6 - LINE OF CREDIT AND NOTES PAYABLE

- A) On May 14, 2015, Leake and Watts obtained a \$5,625,807 term loan from TD Bank, N.A. (TD Bank). The loan matures on June 1, 2025, and is payable in monthly installments of \$57,146 including interest at 4.01%, beginning July 1, 2015. The loan is collateralized by assets held by BNY Mellon in the custodial investment accounts of Leake and Watts. \$ 5,160,824

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**LEAKE AND WATTS SERVICES, INC.
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 6 - LINE OF CREDIT AND NOTES PAYABLE (continued)

B) On May 15, 2015, Leake and Watts obtained a \$5,000,000 revolving line of credit from TD Bank. The revolving line of credit matures on May 15, 2017 and bears interest at the prime rate, which was 3.50% at June 20, 2015. The line of credit is secured by accounts receivable.	\$ -
C) On January 5, 2009, Leake and Watts entered into a mortgage with Castle Combe Associates LLC for \$3,795,737 to purchase a building at 450 Castle Hill Avenue, Bronx. The mortgage is secured by the aforementioned property. Payments of \$28,300 are due monthly through February 1, 2029. The interest rate is 6.50%.	2,913,634
D) On December 15, 2011, Leake and Watts entered into a computer equipment financing agreement with HVB Leasing Corp. in the amount of \$400,000 to upgrade the computer network. Payments of \$7,800 per month are due monthly. The interest rate is 7.49%. The note matures in January 2017. HVB Leasing Corp. has a first-priority security interest in the computer equipment.	53,262
E) On June 27, 2016, Leake and Watts entered into an unsecured property renovation note with Tower Property Management Co., Inc. in the amount of \$165,100 for the partial renovation of the second floor to the property located at Williamsbridge Road, Bronx. Payments of \$5,098, including interest at 7%, are due monthly. The note matures in May 2019.	<u>160,003</u>
	<u>\$ 8,287,723</u>

Payments for the line of credit and all notes payable over the next five years are as follows:

2017	\$ 743,483
2018	725,361
2019	756,234
2020	735,286
2021	770,917
Thereafter	<u>4,556,442</u>
Total	<u>\$ 8,287,723</u>

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**LEAKE AND WATTS SERVICES, INC.
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 6 - LINE OF CREDIT AND NOTES PAYABLE (continued)

In connection with the term loan obtained from TD Bank, Leake and Watts incurred \$60,512 of financing costs. These costs will be amortized over the life of the term loan. The unamortized balance at June 30, 2016 was \$56,797.

In addition, there are certain financial covenants associated with Leake and Watts' lines of credit. As of June 30, 2016, Leake and Watts was in compliance with those covenants.

NOTE 7 - CAPITAL LEASE PAYABLE

Baytree National Bank and Trust Company

In February 2013, Leake and Watts entered into a computer equipment financing agreement with Baytree National Bank and Trust Company in the amount of \$221,535 to finance the purchase of smart boards and audio equipment. Payments of \$4,344 are due monthly. The interest rate is 9.1%. The lease matures in February 2017. The balance outstanding as of June 30, 2016 was \$33,596.

TD Equipment Finance, Inc.

In October 2015, Leake and Watts entered into a \$1,000,000 equipment financing agreement with TD Equipment Finance, Inc. to lease equipment, that will expire on February 28, 2017. In April 2016, Leake and Watts financed the purchase of \$120,568 of equipment. Principal payments of approximately \$2,207 and interest at an annual rate of 3.75% charged on the outstanding balance are due monthly. The lease matures in March 2021. The balance outstanding at June 30, 2016 was \$115,060. \$879,432 was available to finance future purchases at June 30, 2016.

The capital leases are secured by the underlying assets financed. Future lease payments are as follows:

2017	\$ 61,235
2018	26,483
2019	26,483
2020	26,483
2021	<u>19,865</u>
	160,549
Less amount representing interest	<u>(11,893)</u>
Present value of net minimum lease payments	148,656
Less current portion	<u>(56,147)</u>
Long-term obligation under capital lease	<u>\$ 92,509</u>

-continued-

**LEAKE AND WATTS SERVICES, INC.
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 8 - BONDS PAYABLE

Series 2013B-1 and Series 2013B-2

On May 9, 2013, the Dormitory Authority of the State of New York (“DASNY”) issued Series 2013B-1 and Series 2013B-2 Bonds aggregating \$4,035,000 for the purpose of the financing and refinancing of costs incurred in connection with (a) 1035 E. 233rd Street, Bronx (233rd Street) for \$965,000; (b) 634 East 241st Street, Bronx (241st Street) for \$590,000; (c) 954 East 211th Street, Bronx (211th Street) for \$550,000; (d) 1623 Glover Street, Bronx (Glover Street) for \$715,000; (e) 4316 Van Cortland Parkway East, Bronx (Hurst House) for \$640,000; and (f) 450 Castle Hill Avenue, Bronx (Castle Hill) for \$575,000.

One twelfth of the annual principal payment and one sixth of the semiannual interest payment are paid to the bond trustee monthly. The debt service schedule (term of loan) for each Facility coincides with its reimbursement commitment from OPWDD. The principal balance outstanding on the bonds at June 30, 2016 was \$3,465,000.

The bonds are secured by a second mortgage lien on each Facility and a subordinate lien on the Public Funds attributable to the Facilities secured by a Stand-by Intercept Agreement with OPWDD. At June 30, 2016, the amount held in the debt service reserve fund was \$188,225; in the debt service fund was \$333,336; in the construction fund was \$39,491. These amounts are reflected as investments limited as to use on the accompanying statement of financial position. The rate of interest on the bonds ranges from 1.43% to 3.25%.

Bond proceeds from the Series 2013B-1 and 2013B-2 were also used to pay the cost of issuance of the bonds totaling \$256,423 and the bond discount of \$47,860. These costs will be amortized as interest expense over the life of the bonds. At June 30, 2015, the unamortized bond issuance cost was \$203,042. At June 30, 2015, the unamortized bond discount was \$38,288.

Series 2014 Bonds

On June 27, 2014, \$21,173,000 aggregate principal amount of Special Obligation Revenue Bonds were issued pursuant to a certain Bond Purchase and Loan Agreement by and among the Yonkers Economic Development Corporation (the “Issuer”), Leake and Watts Services, Inc. (the “Company”), and BankUnited, Inc., as purchaser of the Bonds (the “Bank”). The component features of the total bond financing are set forth in the table below:

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**LEAKE AND WATTS SERVICES, INC.
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 8 - BONDS PAYABLE (continued)

Series 2014 Bonds (continued)

<u>Series</u>	<u>Original Principal Amount</u>	<u>Balance at June 30, 2016</u>	<u>Maturity</u>	<u>Interest Rate</u>	<u>Price</u>
Series 2014A	\$ 16,670,000	\$ 14,970,000	June 1, 2029	3.330%	100%
Series 2014B	1,240,000	765,000	June 1, 2022	3.550%	100%
Series 2014C	3,125,000	2,730,000	June 1, 2026	4.380%	100%
Series 2014D	<u>138,000</u>	<u>96,000</u>	June 1, 2019	2.980%	100%
	<u>\$ 21,173,000</u>	<u>\$ 18,561,000</u>			

The Bonds were issued for the purpose of providing funds for certain projects for the Company consisting of (i) the refinancing and paying down of old debt and (ii) issuance cost of the Series 2014 Bonds totaling \$871,100. These costs will be amortized over the life of the bonds. At June 30, 2016, the unamortized bond issuance cost was \$709,046.

The 2014 Bonds loan agreement requires principal payments through June 1, 2029, and the maintenance of certain reserve funds. Principal payments are due annually. Interest payments are due semiannually. The principal balance outstanding on the Bonds was \$18,561,000 at June 30, 2016.

The Bonds are special obligations of the Issuer and are payable solely from the revenues, receipts and other payments derived from the loan by the Bank from the Company. As security for the Bonds and the Company's obligations under the Loan Agreement, the Company has granted to the Issuer a first priority mortgage lien and security interest in the Facility pursuant to a certain Mortgage, Assignment of Rents, Security Agreement and Fixture Filing.

Annual debt service amounts payable during the next five years and thereafter are as follows:

2017	\$ 1,606,000
2018	1,649,000
2019	1,686,000
2020	1,690,000
2021	1,760,000
Thereafter	<u>13,635,000</u>
	22,026,000
Less net unamortized discount	<u>(38,288)</u>
Total	<u>\$ 21,987,712</u>

-continued-

**LEAKE AND WATTS SERVICES, INC.
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 9 - POSTRETIREMENT BENEFITS

The present value of Leake and Watts' agreement with the former executive director relating to the provision of health benefits on his family's behalf as of June 30, 2016 was \$33,788. The liability is included in accrued payroll and employee benefits on the accompanying statement of financial position.

In June 2015, Leake and Watts established a trust to accumulate funds that can be used to supplement the executive director's retirement income and to provide additional benefits in the event of the executive director's death or serious illness. To fund the trust, Leake and Watts has agreed to loan the trust \$64,000 in each of the next 5 years but can discontinue payments at its discretion. The loan accrues interest at the prevailing Applicable Federal Rate (AFR) which was 1.41% at June 30, 2016, and will be repaid from either the cash value of the policy or from the proceeds from the life insurance policy upon the executive director's death. The receivable is included in accounts receivable on the accompanying statement of financial position.

NOTE 10 - COMMITMENTS AND CONTINGENCIES

(a) Noncancelable leases principally relate to office space, residential housing, office equipment, and automobiles. These leases expire between July 2015 and December 2029. Minimum payments for the next five years and thereafter are as follows:

2017	\$ 2,784,000
2018	2,679,000
2019	2,311,000
2020	2,197,000
2021	719,000
Thereafter	<u>3,949,216</u>
Total	<u>\$ 14,639,216</u>

(b) Total rent expense, including office equipment and vehicle leases, amounted to \$3,747,979.

(c) During the period from January 2000 to December 2005, workers' compensation coverage was provided by the Provider Agency Trust for Human Services (the "Trust"). In May 2015, Leake and Watts agreed to a settlement of \$562,976, plus interest at 3.5%, resulting in 120 monthly payments of \$5,567 beginning July 2015. As a result of the settlement, Leake and Watts was able to write down their accrued liability by \$207,511. The balance as of June 30, 2016 was \$515,114.

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**LEAKE AND WATTS SERVICES, INC.
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 10 - COMMITMENTS AND CONTINGENCIES (continued)

(c) (continued)

Principal payments over the next five years and thereafter are as follows:

2017	\$ 49,565
2018	51,328
2019	53,154
2020	55,044
2021	57,002
Thereafter	<u>249,021</u>
Total	\$ <u>515,114</u>

- (d) Leake and Watts is involved with third parties in legal matters in which damages and other remedies are sought. Such suits and claims are either specifically covered by insurance or are not material. While the outcome of these suits cannot be determined at this time, management believes that any loss which may arise from these actions will not have a material adverse effect on the financial position or results of operations of Leake and Watts.
- (e) Leake and Watts is responsible for reporting to several third parties. These agencies, as well as the New York State office of the Attorney General, the Internal Revenue Service, the New York State Office of the Medicaid Inspector General and the New York State Department of Charities Registration have the right to audit Leake and Watts.

The eventual liability to governmental agencies, if any, upon final settlement of the open years has not been finalized. However, Leake and Watts has recorded estimated provisions of approximately \$2,411,644 for the eventual settlement of the open cost reporting periods and are included in accrued expenses and other liabilities.

(f) Contracts

- Leake and Watts has been awarded a contract for approximately \$4.9 million annually to operate a Limited Secure Placement program in Brooklyn. This contract is expected to be operational in FY17. This award, which represents a commitment of NYC-ACS to provide funds on a cost reimbursement basis to Leake and Watts, will not be reflected in the financial statements until reimbursable activities have been conducted in accordance with the provisions of the contracts. However the construction costs of approximately \$1,142,000 relating to starting the program have been capitalized and are included in construction in progress in these financial statements.

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**LEAKE AND WATTS SERVICES, INC.
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 11 - TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets are available for the following purposes:

Parent child home program	\$ 116,378
J. Douglas Richards fund	<u>25,000</u>
	<u>\$ 141,378</u>

Net assets were released from restrictions by satisfying the following purposes:

Fire safety	\$ 6,120
Parent child home program	108,185
Branding Grant	<u>163,524</u>
Total net assets released from restrictions	<u>\$ 277,829</u>

NOTE 12 - FUNCTIONAL EXPENSES

Program services	\$ 82,467,408
Management and general	8,287,412
Fundraising (development) expenses	273,428
Direct costs of special events	<u>122,557</u>
Total expenses	<u>\$ 91,150,805</u>

NOTE 13 - CONCENTRATIONS

Leake and Watts' cash accounts are in several financial institutions and, at times, they exceed FDIC insurance limits.

Leake and Watts received approximately 60% of their operating revenues from the City of New York in 2016.

89% of Leake and Watts' accounts receivable is from the City of New York, Westchester County, the State of New York and several municipalities within the State at June 30, 2016.

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**LEAKE AND WATTS SERVICES, INC.
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 14 - PERMANENTLY RESTRICTED NET ASSETS

A. Endowment Funds

General

Leake and Watts' endowment consists of four individual donor-restricted endowment funds as follows:

The **Orphan's Fund** contains the funds formerly held by the Orphans Home and Asylum. The income may be used from time to time as the Board of Directors may designate. Its "historic value" is \$1,557,319.

The **Sevilla Fund** contains the funds formerly held by the Sevilla Home for Children. Its "historic value" is \$527,479. The income from this fund is for maintenance and education, including religious instruction of orphans, half-orphans and dependent girls.

The **Hopewell Fund** stems from the Hopewell Society of Brooklyn and its "historic value" is \$175,826. In brief, the income from this fund is for maintenance and education, including religious instruction of orphans, half-orphans and dependent girls.

The Andrew Peck Memorial Fund (**Peck Fund**) is an endowment created in 1927 with \$100,472. The income is to be spent furthering the education and support of the children who are no longer residing at Leake and Watts.

As required by Generally Accepted Accounting Principles, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

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**LEAKE AND WATTS SERVICES, INC.
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 14 - PERMANENTLY RESTRICTED NET ASSETS (continued)

A. Endowment Funds (continued)

Interpretation of Relevant Law

The Board of Directors of Leake and Watts adopted the New York Prudent Management of Institutional Funds Act (NYPMIFA). NYPMIFA moves away from the “historic dollar value” standard, and permits charities to apply a spending policy to endowments based on certain specified standards of prudence. Leake and Watts is governed by the NYPMIFA spending policy, which establishes a standard maximum prudent spending limit of 7% of the average of its previous five years’ balance. As a result of this interpretation, Leake and Watts classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the organization in a manner consistent with the standards of prudence prescribed by NYPMIFA.

Return Objectives, Strategies Employed and Spending Policy

The objective of Leake and Watts is to generate revenues to support programs, as defined above, while maintaining the principal endowment funds at the original amount designated by the donor. The investment policy to achieve this objective is to invest in low-risk securities. Investment income earned in relation to the endowment funds is recorded as temporarily restricted income and released from restriction upon expenditure for the program for which the endowment fund was established. Restricted investment income earned and expended in the same fiscal year is reflected as unrestricted revenue.

Funds with Deficiencies

There were no funds with deficiencies as of June 30, 2016.

Endowment Net Asset Composition by Type of Fund as of June 30, 2015

The endowment net asset composition of \$2,361,096 consists of permanently donor-restricted funds.

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**LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 14 - PERMANENTLY RESTRICTED NET ASSETS (continued)

A. Endowment Funds (continued)

Changes in Endowment Net Assets for the Year Ended June 30, 2015

	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, beginning of year		\$ 2,361,096	\$ 2,361,096
Interest and dividends	\$ 52,566		52,566
Appropriation of endowment assets for expenditure	<u>(52,566)</u>		<u>(52,566)</u>
Endowment net assets, end of year	<u>\$ -</u>	<u>\$ 2,361,096</u>	<u>\$ 2,361,096</u>

B. Beneficial Interests in Perpetual Trusts

The Emergency Shelter, Inc. has beneficial interests in two perpetual trusts of \$1,436,906 as of June 30, 2016.

NOTE 15 - RETIREMENT PLAN

Leake and Watts offers a 401(k) savings retirement plan, including an employer matching program through ING Life Insurance and Annuity Company, a wholly owned subsidiary of Voya Financial, Inc. Leake and Watts matched 58% of the first 3% of the employee's base salary that an employee contributed to the 401(k) plan. Effective January 8, 2016, the plan was amended to require an employer match of 75% of the first 3% of the employee's base salary that an employee contributes. For the year ended June 30, 2016, Leake and Watts contributed \$275,020 to the 401(k) savings retirement plan.

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**LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2016

NOTE 16 - RELATED PARTIES

During 2016, a board member, and the spouse of another board member were senior officers at a bank which provides banking services for Leake and Watts. Fees and interest paid to the bank were approximately \$84,000 in 2016.

During 2016, the spouse of a board member had a financial interest in Leake and Watts' relationship with ING Life Insurance and Annuity Company (ING). Fees paid to ING were included as a reduction on the investment earnings on the pension assets under management by them.

A board member of Leake and Watts is senior council of a law firm retained by Leake and Watts. Legal fees paid to the law firm for the year ended June 30, 2016 were \$15,552.

LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE

SCHEDULE 1

CONSOLIDATING SCHEDULE OF FINANCIAL POSITION

JUNE 30, 2016

(With Summarized Financial Information for June 30, 2015)

	Leake and Watts Services, Inc.	The Emergency Shelter, Inc.	Eliminations	Total	
				2016	2015
ASSETS					
Current assets					
Cash and cash equivalents	\$ 2,935,183	\$ 156,421		\$ 3,091,604	\$ 2,324,191
Investments	7,237,695			7,237,695	12,106,477
Investments - certificates of deposit		25,000		25,000	25,000
Accounts receivable (net of allowance of \$319,000)	10,157,586	718,875	\$ (718,875)	10,157,586	10,657,638
Other receivable	186,965			186,965	298,122
Prepaid expenses	640,855			640,855	627,809
Accrued investment interest receivable	32,262			32,262	40,729
Total current assets	<u>21,190,546</u>	<u>900,296</u>	<u>(718,875)</u>	<u>21,371,967</u>	<u>26,079,966</u>
Assets limited as to use - investments	<u>639,057</u>			<u>639,057</u>	<u>1,389,032</u>
Other assets					
Investments	2,361,096			2,361,096	861,096
Security deposits	105,727			105,727	36,027
Beneficial interest in perpetual trusts		1,436,906		1,436,906	1,525,574
Deferred financing costs	968,885			968,885	1,072,698
Fixed assets - net	<u>34,202,984</u>			<u>34,202,984</u>	<u>34,153,210</u>
Total other assets	<u>37,638,692</u>	<u>1,436,906</u>		<u>39,075,598</u>	<u>37,648,605</u>
Total assets	<u>\$ 59,468,295</u>	<u>\$ 2,337,202</u>	<u>\$ (718,875)</u>	<u>\$ 61,086,622</u>	<u>\$ 65,117,603</u>

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LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE

SCHEDULE 1

-2-

CONSOLIDATING SCHEDULE OF FINANCIAL POSITION

JUNE 30, 2016

(With Summarized Financial Information for June 30, 2015)

	Leake and Watts Services, Inc.	The Emergency Shelter, Inc.	Eliminations	Total	
				2016	2015
LIABILITIES AND NET ASSETS					
Current liabilities					
Accounts payable	\$ 3,277,851			\$ 3,277,851	\$ 3,381,699
Accounts payable - construction					623,244
Accrued payroll and employee benefits	3,962,620			3,962,620	2,869,078
Accrued expenses and other liabilities	4,356,413	\$ 20,525	\$ (718,875)	3,658,063	3,141,466
Advances from government agencies	2,117,721			2,117,721	4,775,822
Accrued interest payable	42,744			42,744	45,544
Line of credit and notes payable	743,483			743,483	2,713,790
Capital leases payable	56,147			56,147	46,737
Bonds payable - net	1,606,000			1,606,000	1,689,000
Total current liabilities	<u>16,162,979</u>	<u>20,525</u>	<u>(718,875)</u>	<u>15,464,629</u>	<u>19,286,380</u>
Long-term liabilities					
Accrued payroll and employee benefits	465,549			465,549	515,113
Line of credit and notes payable	7,544,240			7,544,240	8,127,690
Capital leases payable	92,509			92,509	33,596
Bonds payable - net	20,381,712			20,381,712	21,984,522
Total long-term liabilities	<u>28,484,010</u>			<u>28,484,010</u>	<u>30,660,921</u>
Total liabilities	<u>44,646,989</u>	<u>20,525</u>	<u>(718,875)</u>	<u>43,948,639</u>	<u>49,947,301</u>
Net assets (Schedule 2)					
Unrestricted	12,318,832	879,771		13,198,603	10,980,803
Temporarily restricted	141,378			141,378	302,829
Permanently restricted	2,361,096	1,436,906		3,798,002	3,886,670
Total net assets	<u>14,821,306</u>	<u>2,316,677</u>		<u>17,137,983</u>	<u>15,170,302</u>
Total liabilities and net assets	<u>\$ 59,468,295</u>	<u>\$ 2,337,202</u>	<u>\$ (718,875)</u>	<u>\$ 61,086,622</u>	<u>\$ 65,117,603</u>

See independent auditor's report.

LEAKE AND WATTS SERVICES, INC.
AND AFFILIATE

SCHEDULE 2

CONSOLIDATING SCHEDULE OF ACTIVITIES

YEAR ENDED JUNE 30, 2016
(With Summarized Financial Information
for the Year Ended June 30, 2015)

	2016									2015
	Leake and Watts Services, Inc.			The Emergency Shelter, Inc.		Eliminations	Total			Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	Unrestricted	Permanently Restricted		Unrestricted	Temporarily Restricted	Permanently Restricted	
Operating revenues										
Program revenue	\$ 86,299,264						\$ 86,299,264		\$ 86,299,264	\$ 81,139,330
In-kind contributions	470,609						470,609		470,609	637,985
Program development grant	4,347,952						4,347,952		4,347,952	
Total operating revenues	91,117,825						91,117,825		91,117,825	81,777,315
Operating expenses										
Program services	82,467,408			\$ 75,000		\$ (75,000)	82,467,408		82,467,408	76,740,065
Supporting services										
Management and general	8,225,188			3,914		(13,618)	8,215,484		8,215,484	6,396,899
Development	273,428						273,428		273,428	223,644
Total supporting services	8,498,616			3,914		(13,618)	8,488,912		8,488,912	6,620,543
Total operating expenses	90,966,024			78,914		(88,618)	90,956,320		90,956,320	83,360,608
Change in net assets from operations	151,801			(78,914)		88,618	161,505		161,505	(1,583,293)
Nonoperating revenues										
Investment income (loss)	(13,017)			13,618		(13,618)	(13,017)		(13,017)	333,926
Capital improvement grant	645,974						645,974		645,974	
Contributions	795,793	\$ 116,378		72,511		(75,000)	793,304	\$ 116,378	909,682	971,647
Special events	474,647						474,647		474,647	621,668
Direct costs of special events	(122,557)						(122,557)		(122,557)	(109,702)
Change in value of beneficial interest in perpetual trusts					\$ (88,668)			\$ (88,668)	(88,668)	23,973
Miscellaneous income				115			115		115	133
Net assets released from restrictions	277,829	(277,829)					277,829	(277,829)		
Change in net assets (Exhibit C)	2,210,470	(161,451)		7,330		(88,668)	2,217,800	(161,451)	(88,668)	1,967,681
Net assets - beginning of year	10,108,362	302,829	\$ 2,361,096	872,441	1,525,574		10,980,803	302,829	3,886,670	15,170,302
Net assets - end of year	\$ 12,318,832	\$ 141,378	\$ 2,361,096	\$ 879,771	\$ 1,436,906	\$ -	\$ 13,198,603	\$ 141,378	\$ 3,798,002	\$ 15,170,302

See independent auditor's report.

CONSOLIDATED SCHEDULE OF FUNCTIONAL EXPENSES

YEAR ENDED JUNE 30, 2016
(With Summarized Financial Information
for the Year Ended June 30, 2015)

	2016						2015				
	Program Services					Total	Supporting Services			Total	
	Child Welfare	Special Education	Developmental Disabilities	Early Childhood	Juvenile Justice		Management and General	Development	Direct Costs of Special Events		
Employee compensation and benefits											
Salaries and wages	\$ 16,391,030	\$ 10,271,638	\$ 7,056,647	\$ 6,732,484	\$ 5,871,382	\$ 46,323,181	\$ 3,452,088	\$ 147,357	\$ 3,599,445	\$ 49,922,626	\$ 47,183,123
Fringe benefits	4,799,693	2,966,118	2,052,962	1,970,456	1,734,085	13,523,314	1,015,499	44,730	1,060,229	14,583,543	14,261,281
Total employee compensation and benefits	21,190,723	13,237,756	9,109,609	8,702,940	7,605,467	59,846,495	4,467,587	192,087	4,659,674	64,506,169	61,444,404
Specific assistance to individuals											
Payments to foster parents	2,091,939					2,091,939				2,091,939	2,305,773
Food	409,033	80,198	210,037	188,722	344,900	1,232,890				1,232,890	1,078,574
Children's allowances and activities	966,745	103,271	99,713	13,930	156,755	1,340,414				1,340,414	858,820
Consumer incidentals	25,056		709		23,164	48,929				48,929	51,199
Clothing	81,217		15,591	713	18,178	115,699				115,699	101,533
Total specific assistance to individuals	3,573,990	183,469	326,050	203,365	542,997	4,829,871				4,829,871	4,395,899
Occupancy											
Interest expense	168,711	290,718	305,066	141,139	402	906,036	380,901	1,574	382,475	1,288,511	1,087,046
Rent	505,579	782,768	293,419	1,184,636	322,495	3,088,897				3,088,897	2,695,388
Utilities	365,186	425,758	227,256	182,837	110,664	1,311,701		1,593	60,948	1,372,649	1,419,430
Maintenance and repairs	143,434	67,784	86,332	92,547	139,857	529,954	60,663		60,663	590,617	577,576
Security	89,158	35,568	74,915	24,018	97,028	320,687	36,607	1,684	38,291	358,978	258,529
Janitorial services	61,421	60,992	43,066	27,525	7,643	200,647	109,019	2,524	111,543	312,190	189,176
Total occupancy	1,333,489	1,663,588	1,030,054	1,652,702	678,089	6,357,922	646,545	7,375	653,920	7,011,842	6,227,145
Professional fees											
Clinical services	532,122		385	305,780	68,725	907,012				907,012	924,125
Legal and audit	228,751	194,560	18,783	32,474	35,944	510,512	129,751		129,751	640,263	587,935
Other independent contractors	386,201	357,426	120,375	610,009	91,169	1,565,180	671,734	4,023	675,757	2,240,937	1,868,600
Total professional fees	1,147,074	551,986	139,543	948,263	195,838	2,982,704	801,485	4,023	805,508	3,788,212	3,380,660
Other											
Supplies	566,522	803,433	154,270	193,802	204,164	1,922,191	150,319	31,357	\$ 13,200	194,876	2,117,067
Transportation and other travel-related expenses	419,168	20,460	216,769	14,412	47,544	718,353	57,559	5,603	63,162	781,515	713,387
Insurance	339,887	326,991	182,869	118,104	89,647	1,057,498	118,382	2,462	120,844	1,178,342	1,107,324
Telephone	174,439	245,523	129,295	77,775	71,604	698,636	99,029	1,187	100,216	798,852	628,763
Vehicle rentals, repairs and replacement	162,166	24,798	202,100	558	50,759	440,381	22,577		22,577	462,958	395,735
Equipment/furniture rentals, repairs and replacement	117,820	91,245	73,758	92,522	36,882	412,227	106,496	5,794	112,290	524,517	405,519
Staff development	216,174	15,227	21,837	59,553	263,409	576,200	84,477	150	84,627	660,827	489,870
Staff recruitment	87,262	49,498	38,064	57,472	16,951	249,247	36,637	2,493	39,130	288,377	111,272
Printing, postage, subscriptions, publications	9,088	18,812	539	587	1,230	30,256	50,140	15,151	65,291	95,547	78,230
Dues, licenses, permits	17,886	3,732	771	9,476	175	32,040	102,463	2,214	104,677	136,717	70,083
Line of credit interest expense							120,139		120,139	120,139	113,476
Investment management fees							71,928		71,928	71,928	66,383
Bad debt							1,020,573		1,020,573	1,020,573	
Miscellaneous	15,144	747	39,058	6,643	8,081	69,673	42,385		109,357	151,742	325,325
Total other	2,125,556	1,600,466	1,059,330	630,904	790,446	6,206,702	2,083,104	66,411	122,557	2,272,072	5,952,725
Total expenses before depreciation and amortization	29,370,832	17,237,265	11,664,586	12,138,174	9,812,837	80,223,694	7,998,721	269,896	122,557	8,391,174	88,614,868
Depreciation and amortization	547,432	572,670	549,543	103,994	470,075	2,243,714	288,691	3,532	292,223	2,535,937	2,135,860
Total expenses	29,918,264	17,809,935	12,214,129	12,242,168	10,282,912	82,467,408	8,287,412	273,428	122,557	8,683,397	91,150,805
Less expenses deducted directly from revenues on the consolidated statement of activities											
Investment management fees							(71,928)		(71,928)	(71,928)	(66,383)
Direct cost of special events								(122,557)	(122,557)	(122,557)	(109,702)
Total expenses reported by function on the consolidated statement of activities	\$ 29,918,264	\$ 17,809,935	\$ 12,214,129	\$ 12,242,168	\$ 10,282,912	\$ 82,467,408	\$ 8,215,484	\$ 273,428	\$ -	\$ 8,488,912	\$ 90,956,320

See independent auditor's report.